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July 29, 2003

VIA ELECTRONIC FILING

Ms. Marlene H. Dortch
Secretary
Federal Communications Commission
445 Twelfth Street, S. W. – Room TWB-204
Washington, D. C. 20554

Re: *Ex parte,* CC Docket No. 96-149, Verizon Petition for Forbearance from the Prohibition of sharing Operating, Installation, and Maintenance Functions Under Section 53.203(a)(2) of the Commission's Rules

Dear Ms. Dortch:

On Tuesday, July 29, 2003, Aryeh Friedman and the undersigned of AT&T met with William Dever, Robert Tanner, and Pamela Megna of the Wireline Competition Bureau's Competition Policy Division and Andrea Kearney of the Office of the General Counsel. The purpose of the meeting was to review AT&T's July 9, 2003 written ex parte submissions in the above-captioned proceeding. These submissions respond to Verizon's arguments regarding the Commission's forbearance authority under section 10(d) of the Communications Act and the costs that are purportedly caused by the Commission's rules prohibiting the sharing of operating, installation and maintenance services between a Bell Operating Company and its section 272 separate affilitate. The attached outline was distributed at the meeting to facilitate our discussion.

Consistent with Section 1.1206 of the Commission's rules, I am filing one electronic copy of this notice and request that you place it in the record of the above-captioned proceeding.

Sincerely,

F S Simone

ATTACHMENT

cc: W. Dever
A. Kearney
P. Megna
R. Tanner

Verizon's "Cost Analysis"

1. Even if the Commission could forbear under Section 10(d) (which it cannot for the reasons set forth in our White Paper) Verizon's "cost analysis" is irrelevant under section 10 because the OI&M rules are "necessary" to prevent "unjust[] and unreasonably discriminatory" practices by Verizon, and "for the protection of consumers – that is, there is a "strong connection" between those safeguards and the protection of long distance competition, and therefore the Commission cannot forbear regardless of the costs. *Cellular Telecommunications & Internet Assoc. v. FCC*, No. 02-1264, slip op. at 17 (D.C. Cir. June 6, 2003)

2. Even if a cost analysis were relevant, Verizon's "cost support" does not establish any "record" basis to support its (improperly captioned) "Forbearance Petition" because it is irreproducible and undocumented and therefore cannot be independently validated. *E.g., AT&T Corp. v. Business Telecom, Inc.* 16 FCC Rcd. 12312, ¶ 49 (2001). The core of Verizon's "analysis" – a table that lists unverifiable percentages of expenses for various categories (*e.g.*, OSS, workforce) that Verizon claims are driven by the Commission's OI&M rules. Verizon then applies these arbitrary figures to the total expenses Verizon claims that its section 272 affiliate (GNI) incurs for each expense category, with the results of that multiplication being the claimed overall "cost savings."

What Verizon should have submitted:

(a) Workpapers and all data, analyses and documentation, including financial reports, underlying its cost savings calculations should have been provided. Sufficient data to be able to verify and test Verizon's assumptions, such as, for example, labor rates, capital costs, depreciation lives, and whether the costs in question are actually "driven" by section 272 and the prohibition on OI&M sharing in particular.

(b) Affidavits by each of the subject matter experts consulted setting forth: (i) their background and area of expertise; (ii) what they looked at and relied upon; (iii) how the specific numerical values of the various percentages had been arrive at; (iv) what facts they relied upon, (v) what analyses they conducted, and (vi) what efforts they made to examine and verify the reasonableness of the "assumptions" that had been utilized.

3. Verizons's "absorption" theory: (i) demonstrates its incentive and ability to misallocate costs even under price cap regulation, (ii) is contrary to TELRIC-based pricing and (iii) runs counter to the cost allocation requirement of 47 CFR § 64:

(a) Verizons's "absorption" theory: Verizon calculated how much GNI would purportedly save if Verizon's BOCs were able to provide OI&M on its behalf, but did not consider the corresponding cost increases that the BOC would incur in taking over these functions, *i.e.*, Verizon did not determine how *overall* firm-wide costs would be changed. Verizon assumes that its BOC has so much excess capacity that it could "absorb" the incremental work without any incremental cost.

(b) This is inconsistent with the assumption that *price cap* ILECs are operating efficiently. Verizon has represented to the Commission and state PUCs that its realized earnings levels for price capped services has deteriorated, as evidence that the X-factors in those plans are set too high and should be reduced or eliminated altogether. If there is excess capacity, that would explain the low productivity growth and would have resulted in higher rates for monopoly services. Verizon's effort to shift this excess ILEC capacity to the uncompensated benefit of its Section 272 affiliates is an *unlawful cross-subsidy* of the competitive services being provided by the affiliates funded by excessive prices for Verizon's regulated monopoly ILEC services.

(c) Verizon's "absorption" theory would ascribe to GNI no more than the short-run incremental cost of the integrated OI&M functions, which would be less than TELRIC-based prices that Verizon charges to its CLEC competitors for unbundled access to its network.

(d) Verizon's "absorption" theory runs counter to the cost allocation requirement of 47 CFR § 64, which requires apportionment of costs between regulated and non-regulated ILEC services on the basis of fully distributed cost. If excess capacity is present, the Commission's cost allocation rules would require that the costs of the excess capacity be spread ratably across all utilized capacity, rather than being made available, without charge, to the non-regulated affiliate.

4. Much of the savings Verizon seeks to ascribe to OI&M integration arises from the Verizon Section 272 affiliate bypassing the inefficient ordering/provisioning processes (the formal ASR/LSR transmittals) that the BOCs have required competing IXCs to follow, giving its 272 affiliates superior and *discriminatory* direct access to its systems and personnel not available to its nonaffiliated rivals.

5. Verizon has *voluntarily* created five different section 272 affiliates, each with its own OI&M resources; two – Verizon Global Solutions and Verizon Global Networks, Inc. – apparently own switching facilities in the same city. This belies Verizon's claims that the OI&M rules impose prohibitive costs. Significant cost savings could be achieved by integrating the five separate 272 entities into one single unit; under Verizon's "absorption" theory, Verizon's other 272 affiliates could have sufficient capacity to handle GNI's OI&M. Note also that New York already allowed to integrate OI&M so those "costs" should be deducted.